

CITY OF SUMMERSET
SUMMERSET, SOUTH DAKOTA

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT
DECEMBER 31, 2008

CITY OF SUMMERSET

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INDEPENDENT AUDITOR'S REPORT

City Council
City of Summerset
Summerset, South Dakota

We have audited the accompanying cash basis financial statements of governmental activities, the business-type activities, and each major fund of the **CITY OF SUMMERSET** (the City), Meade County, South Dakota, as of and for the year ended December 31, 2008, which collectively comprise the City's basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the City prepares its financial statements on the cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

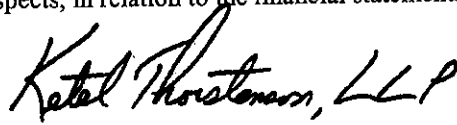
In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position-cash basis of the governmental activities, the business-type activities, and each major fund of the City, as of December 31, 2008, and the respective changes in financial position-cash basis, thereof and for the year then ended in conformity with the basis of accounting described in Note 1.

In accordance with Government Auditing Standards, we have also issued our report dated February 1, 2010, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards, and should be considered in assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages 3 through 7, and 24 through 26 are not a required part of the basic financial statements but are supplementary information required to accompany those financial statements. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

City Council

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-profit Organizations, and is not a required part of the basic financial statements of the City. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

A handwritten signature in black ink that reads "Ketel Thorstenson, LLP". The signature is stylized with a large, looped initial 'K' and a trailing 'P'.

KETEL THORSTENSON, LLP
Certified Public Accountants

February 1, 2010

CITY OF SUMMERSET

MANAGEMENT'S DISCUSSION AND ANALYSIS DECEMBER 31, 2008

Our discussion and analysis of the City of Somerset's (the City) financial performance provides an overview of the City's financial activities for the year ended December 31, 2008, within the limitations of the City's cash basis of accounting. We encourage readers to consider it in conjunction with the City's financial statements.

FINANCIAL HIGHLIGHTS

The City's total debt increased by approximately \$3,300,000 during the year ended December 31, 2008 due to the purchase of the Somerset Wastewater Treatment Plant. This project was funded through a USDA Rural Development Loan. Repayment will be through monthly sewer charges and property tax revenue from the newly formed Tax Increment District #1.

The City continued to work on Public Works projects during 2008. Those projects included street light installation, street repairs, and drainage improvements. (Approximately \$260,000).

The City also hired a full time police officer, purchased two police vehicles, and purchased needed law enforcement equipment and supplies to sufficiently equip the newly formed department (approximately \$119,000).

USING THIS ANNUAL REPORT

This annual report is presented in a format consistent with the presentation requirements of the Governmental Accounting Standards Board (GASB) Statement No. 34, as applicable to the City's cash basis of accounting.

Report Components

This annual report consists of four parts as follows:

Government-Wide Financial Statements: The Statement of Net Assets and the Statement of Activities provide information about the activities of the City using a government-wide focus (or "as a whole").

Fund Financial Statements: Fund financial statements focus on the individual parts of City government. Fund financial statements also report the City's operations in more detail than the government-wide statements by providing information about the City's most significant ("major") funds. For *governmental activities*, these statements tell how these services were financed in the short term, as well as what remains for future spending. For *proprietary activities*, these statements offer financial information about the activities the City operates like businesses, such as water, sewer, and solid waste services.

Notes to the Financial Statements: The notes to the financial statements are an integral part of the government-wide and fund financial statements and provide expanded explanation and detail regarding the information reported in the statements.

Required Supplementary Information: This Management's Discussion and Analysis and the Budgetary Comparison Schedules represent financial information required to be presented by GASB. Such information provides users of this report with additional data that supplements the government-wide statements, fund financial statements, and notes (referred to as "the basic financial statement"). The Budgetary Comparison Schedule is presented on a budgetary basis of accounting, whereby capital outlay expenditures are reported within the respective functions rather than as a separate capital outlay function.

Basis of Accounting

The City has elected to present its financial statements on a cash basis of accounting. This cash basis of accounting is a basis of accounting other than generally accepted accounting principles. Basis of accounting is a reference to *when* financial events are recorded, such as the timing for recognizing revenues, expenses, and their related assets and liabilities. Under the City's cash basis of accounting, revenues and expenses, and related assets are recorded when they result from cash transactions.

CITY OF SUMMERSET

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED) DECEMBER 31, 2008

USING THIS ANNUAL REPORT (CONTINUED)

Basis of Accounting (Continued)

As a result of the use of this cash basis of accounting, certain assets and their related revenues, (such as accounts receivable and revenue for billed or provided services not yet collected) and liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) *are not recorded* in these financial statements. Therefore, when reviewing the financial information and discussion within this annual report, the reader should keep in mind the limitations resulting from the use of the cash basis of accounting.

Reporting the City as a Whole

The City's Reporting Entity Presentation

This annual report includes all activities for which the City of Somerset City Council is fiscally responsible. These activities, defined as the City's reporting entity, are operated within separate legal entities that make up the primary government. The primary government includes the legal entity of the City of Somerset.

The Government-Wide Statement of Net Assets and the Statement of Activities

One of the most important questions asked about the City's finances is, "Is the City as a whole better off or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Activities report information about the City as a whole and about its activities in a way that helps answer this question. These statements include all of the City's assets resulting from the use of the cash basis of accounting.

These two statements report the City's net assets and changes in them. Keeping in mind the limitations of the cash basis of accounting, you can think of the City's net assets as one way to measure the City's financial health or financial position. Over time, increases or decreases in the City's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the City's sales tax base and the condition of the City's roads, to assess the overall health of the City.

In the Statement of Net Assets and the Statement of Activities, we divide the City into two kinds of activities:

Governmental activities. Most of the City's basic services are reported here, including the police, general government, streets and parks. Sales taxes, property taxes and state and federal grants finance most of these activities.

Business-type activities. The City charges a fee to customers to help it cover all or most of the cost of certain services it provides. The City's sewer system is reported here.

Reporting the City's Most Significant Funds

The Fund Financial Statements

The fund financial statements provide detailed information about the most significant funds, not the City as a whole. Some funds are required to be established by State law and by bond covenants. However, the City Council establishes certain other funds to help it control and manage money for particular purposes or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money. The City has two kinds of funds - *Governmental and Proprietary.*

CITY OF SUMMERSET

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2008

USING THIS ANNUAL REPORT (CONCLUDED)

Reporting the City's Most Significant Funds (Continued)

The Fund Financial Statements (Continued)

Governmental funds - Most of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds report the acquisition of capital assets and payments for debt principal as expenditures and not as changes to asset and debt balances. The governmental fund statements provide a detailed short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps you determine (through a review of changes to fund balance) whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. The City considers the General Fund and Tax Increment District #1, Debt Service Fund, to be its significant or major governmental funds.

Proprietary funds - When the City charges customers for the services it provides, these services are generally reported in proprietary funds. The City's proprietary (enterprise) fund financial statements are essentially the same as the business-type activities we report in the government-wide statements, but the fund statements provide more detail and additional information. The Sewer Fund is the only proprietary fund of the City.

A FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net Assets – Cash Basis

Since this is the first year to report all activities on the cash basis of accounting, a comparison to the prior year is not possible. However, in future years, this section will explain the differences between the current and prior year figures. The City's combined net assets, resulting from cash basis transactions are as follows:

	Governmental Business-Type		Totals
	Activities	Activities	
	<u>2008</u>	<u>2008</u>	<u>2008</u>
ASSETS:			
Cash and Cash			
Equivalents	\$ 177,431	\$ 11,849	\$ 189,280
Restricted Assets:			
Cash and Cash			
Equivalents	5,169	-	5,169
TOTAL ASSETS	\$ 182,600	\$ 11,849	\$ 194,449
NET ASSETS:			
Restricted	\$ 5,169	\$ -	\$ 5,169
Unrestricted	177,431	11,849	189,280
TOTAL NET ASSETS	\$ 182,600	\$ 11,849	\$ 194,449

CITY OF SUMMERSET

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2008

A FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Assets-Cash Basis

For the year ended December 31, 2008, net assets of the primary government (resulting from cash basis transactions) are as follows:

	Governmental Activities 2008	Business-Type Activities 2008	Totals 2008
Program Revenues			
Charges for Services	\$ 48,581	\$ 40,338	\$ 88,919
Operating Grants and Contributions	42,553	-	42,553
Capital Grants and Contributions	1,720	-	1,720
General Revenues			
Property Tax	419,465	-	419,465
Sales Tax	212,627	-	212,627
State Shared Revenues	23,896	-	23,896
Investment Income	16	-	16
Debt Issued	3,307,500	-	3,307,500
Miscellaneous	10,739	-	10,739
Total Revenues	4,067,097	40,338	4,107,435
Expenses			
General Government	209,163	-	209,163
Public Safety	153,415	-	153,415
Public Works	3,525,871	-	3,525,871
Health and Welfare	1,104	-	1,104
Conservation and Development	25,150	-	25,150
Sewer	-	23,320	23,320
Debt Service	107,500	-	107,500
Total Expenses	4,022,203	23,320	4,045,523
Transfers	5,169	(5,169)	-
Change in Net Assets	50,063	11,849	61,912
Ending Net Assets	\$ 182,600	\$ 11,849	\$ 194,449

CITY OF SUMMERSET

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED) DECEMBER 31, 2008

A FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONCLUDED)

Governmental Activities

To aid in the understanding of the Statement of Activities, some additional explanation is given. Of particular interest is the format that is significantly different from a typical Statement of Revenue, Expenses, and Changes in Fund Balance. You will notice that expenses are listed in the first column, with revenues from that particular program reported to the right. The result is a Net (Expense)/Revenue. This type of format highlights the relative financial burden of each of the functions on the City's taxpayers. It also identifies how much each function draws from the general revenues or if it is self-financing through fees and grants or contributions. All other governmental revenues are reported as general. It is important to note that all taxes are classified as general revenue, even if restricted for a specific purpose.

For the year ended December 31, 2008, total expenses for governmental activities, resulting from cash basis transactions, amounted to \$822,203.

Business-Type Activities

For fiscal year 2008, the sewer fund reported net revenues/(expenses) of \$17,018.

A FINANCIAL ANALYSIS OF THE CITY'S FUNDS

Certain funds experienced noteworthy changes from the prior year and are highlighted as follows:

- On the cash basis of accounting, the General Fund reported revenues of \$759,597 and expenditures and net transfers of \$822,203.
- The Sewer Fund reported net assets of \$11,849 in 2008.

General Fund Budgetary Highlights

There were no significant budgetary changes and no significant budget variances in the general fund during the year.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

For the upcoming year ending December 31, 2009, the City's budget is fairly consistent with the 2008 budget.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designated to provide a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional financial information contact the City of Summerset, Finance Officer, 7055A Leisure Lane, Summerset, SD 57718.

CITY OF SUMMERSET

STATEMENT OF ACTIVITIES - CASH BASIS
FOR THE YEAR ENDED DECEMBER 31, 2008

Functions/Programs	Expenses	----- Program Revenues -----			----- Net (Expense) Revenue and -----		
		Charges for	Operating	Capital	Governmental	Business-Type	Total
		Services	Grants and	Grants and	Activities	Activities	
			Contributions	Contributions			
Primary Government:							
Governmental Activities:							
General Government	\$ 209,163	\$ 400	\$ -	\$ -	\$ (208,763)	\$ -	\$ (208,763)
Public Safety	153,415	-	-	1,720	(151,695)	-	(151,695)
Public Works	3,525,871	48,181	42,553	-	(3,435,137)	-	(3,435,137)
Culture and Recreation	1,104	-	-	-	(1,104)	-	(1,104)
Conservation and							
Development	25,150	-	-	-	(25,150)	-	(25,150)
Debt Service	107,500	-	-	-	(107,500)	-	(107,500)
Total Governmental Activities	4,022,203	48,581	42,553	1,720	(3,929,349)	-	(3,929,349)
Business-Type Activity:							
Sewer	23,320	40,338	-	-	-	17,018	17,018
Total Business-Type Activities	23,320	40,338	-	-	-	17,018	17,018
Total Primary Government	\$ 4,045,523	\$ 88,919	\$ 42,553	\$ 1,720	(3,929,349)	17,018	(3,912,331)
General Revenues:							
Taxes:							
Property Taxes					419,465	-	419,465
Sales Taxes					212,627	-	212,627
State Shared Revenues					23,896	-	23,896
Unrestricted Investment Earnings					16	-	16
Miscellaneous Revenue					10,739	-	10,739
Debt Issued					3,307,500	-	3,307,500
Transfers					5,169	(5,169)	-
Total General Revenues and Transfers					3,979,412	(5,169)	3,974,243
Change in Net Assets					50,063	11,849	61,912
Net Assets-January 1, 2008					132,537	-	132,537
Net Assets-December 31, 2008					\$ 182,600	\$ 11,849	\$ 194,449

The accompanying notes are an integral part of this statement.

CITY OF SUMMERSET

**BALANCE SHEET - CASH BASIS
GOVERNMENTAL FUNDS
DECEMBER 31, 2008**

	General Fund	Tax Increment District #1 - Debt Service Fund	Total Governmental Funds
ASSETS:			
101 Cash and Cash Equivalents	\$ 177,431	\$ -	\$ 177,431
107.1 Restricted Cash and Cash Equivalents	-	5,169	5,169
TOTAL ASSETS	\$ 177,431	\$ 5,169	\$ 182,600
FUND BALANCES			
<i>Unreserved Fund Balance</i>			
262.09 Undesignated	\$ 177,431	\$ 5,169	\$ 182,600
TOTAL FUND BALANCES	\$ 177,431	\$ 5,169	\$ 182,600

The accompanying notes are an integral part of this statement.

CITY OF SUMMERSET

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
CASH BASIS - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	General Fund	Tax Increment District #1 - Capital Projects Fund	Tax Increment District #1 - Debt Service Fund	Total Governmental Funds
Revenue:				
<i>310 Taxes:</i>				
311 General Property Taxes	\$ 397,668	\$ -	\$ -	\$ 397,668
313 General Sales and Use Taxes	212,627	-	-	212,627
315 Amusement Taxes	16,577	-	-	16,577
319 Penalties and Interest on Delinquent Taxes	5,220	-	-	5,220
320 Licenses and Permits	45,894	-	-	45,894
<i>330 Intergovernmental Revenue:</i>				
334 State Grants	1,720	-	-	1,720
<i>335 State Shared Revenue:</i>				
335.03 Liquor Tax Reversion	8,323	-	-	8,323
335.04 Motor Vehicle Licenses (5%)	14,263	-	-	14,263
335.08 Local Government Highway and Bridge Fund	1,310	-	-	1,310
<i>338 County Shared Revenue:</i>				
338.99 Other	3,540	-	-	3,540
<i>340 Charges for Goods and Services:</i>				
341 General Government	400	-	-	400
<i>350 Fines and Forfeits:</i>				
351 Court Fines and Costs	2,287	-	-	2,287
<i>360 Miscellaneous Revenue:</i>				
361 Investment Earnings	16	-	-	16
363.01 Principal Collected by County	2,600	-	-	2,600
364.01 Maintenance Assessments	36,413	-	-	36,413
369 Other	10,739	-	-	10,739
Total Revenue	759,597	-	-	759,597

CITY OF SUMMERSET

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
CASH BASIS - GOVERNMENTAL FUNDS (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 2008

	General Fund	Tax Increment District #1 - Capital Projects Fund	Tax Increment District #1 - Debt Service Fund	Total Governmental Funds
Expenditures:				
<i>410 General Government:</i>				
411 Legislative	38,240	-	-	38,240
412 Executive	27,553	-	-	27,553
414 Financial Administration	112,352	-	-	112,352
419 Other	31,018	-	-	31,018
<i>420 Public Safety:</i>				
421 Police	112,304	-	-	112,304
<i>430 Public Works:</i>				
431 Highways and Streets	308,046	-	-	308,046
432 Sanitation	17,825	-	-	17,825
<i>450 Culture and Recreation:</i>				
451 Recreation	1,100	-	-	1,100
452 Parks	4	-	-	4
<i>460 Conservation and Development:</i>				
465 Planning and Zoning	25,150	-	-	25,150
<i>470 Debt Service Costs</i>	-	-	107,500	107,500
<i>485 Capital Outlay</i>	41,111	3,200,000	-	3,241,111
Total Expenditures	714,703	3,200,000	107,500	4,022,203
Other Financing Sources:				
391.01 Transfers In	-	-	5,169	5,169
391.20 Long-Term Debt Issued	-	3,200,000	107,500	3,307,500
Total Other Financing Sources	-	3,200,000	112,669	3,312,669
Net Change in Fund Balances	44,894	-	5,169	50,063
Fund Balances - January 1, 2008	132,537	-	-	132,537
Fund Balances - December 31, 2008	\$ 177,431	\$ -	\$ 5,169	\$ 182,600

The accompanying notes are an integral part of this statement.

CITY OF SUMMERSET

**BALANCE SHEET - CASH BASIS
PROPRIETARY FUNDS
DECEMBER 31, 2008**

	Sewer Fund
ASSETS:	
Current Assets:	
101 Cash and Cash Equivalents	\$ 11,849
TOTAL ASSETS	\$ 11,849

NET ASSETS:	
253.90 Unrestricted Net Assets	\$ 11,849
TOTAL NET ASSETS	\$ 11,849

The accompanying notes are an integral part of this statement.

CITY OF SUMMERSET

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND
NET ASSETS - CASH BASIS - PROPRIETARY FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Sewer Fund
Operating Revenue:	
380 Charges for Goods and Services	\$ 40,338
Total Operating Revenues	40,338
Operating Expenses:	
410 Personal Services	8,278
420 Other Current Expense	15,042
Total Operating Expenses	23,320
Operating Loss	17,018
Transfers	
511 Transfers Out	(5,169)
Change in Net Assets	11,849
Net Assets - January 1, 2008	-
Net Assets - December 31, 2008	\$ 11,849

The accompanying notes are an integral part of this statement.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As discussed further in Note 1.c, these financial statements are presented on a cash basis of accounting. The cash basis of accounting differs from accounting principles generally accepted in the United States of America (GAAP). Generally accepted accounting principles include all relevant Governmental Accounting Standards Board (GASB) pronouncements. In the government-wide financial statements and the fund financial statements for proprietary funds, Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued after November 30, 1989 have not been applied.

a. Financial Reporting Entity:

The reporting entity of the City of Somerset, (the City) consists of the primary government, which includes all of the funds, organizations, institutions, agencies, departments, and offices that make up the legal entity; those organizations for which the primary government is financially accountable; and other organizations for which the nature and significance of their relationship with the primary government are such that their exclusion would cause the financial reporting entity's financial statements to be misleading or incomplete.

b. Basis of Presentation:

Government-wide Financial Statements:

The Statement of Net Assets and Statement of Activities display information about the reporting entity as a whole. These statements include all funds of the reporting entity. The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services.

The statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by recipients of goods and services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

b. Basis of Presentation (Continued):

Fund Financial Statements:

Fund financial statements of the reporting entity are organized into funds, each of which is considered to be a separate accounting entity. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues, and expenditures/expenses. Funds are organized into two major categories: governmental and proprietary. An emphasis is placed on major funds within the governmental and proprietary categories. A fund is considered major if it is the primary operating fund of the City or it meets the following criteria:

1. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least 10 percent of the corresponding total for all funds of that category or type, and
2. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least 5 percent of the corresponding total for all governmental and enterprise funds combined, or
3. Management has elected to classify one or more governmental or enterprise funds as major for consistency in reporting from year to year, or because of public interest in the fund's operations.

The funds of the City financial reporting entity are described below:

Governmental Funds:

General Fund – the General Fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund. The General Fund is always considered to be a major fund.

Debt Service Funds – debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs.

Tax Increment District #1 Debt Service Fund – to account for the property tax revenue received on the tax increment districts to finance debt service related to infrastructure purchases made within the tax increment district. This fund is a major fund.

Capital Projects Funds – capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds or trust funds for individuals, private organizations, or other governments).

Tax Increment District #1 Capital Projects Fund – to account for financial resources to be used for the acquisition of a wastewater treatment plant. This fund is a major fund.

Proprietary Funds:

Enterprise Funds – enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

b. Basis of Presentation (Concluded):

Proprietary Funds (Continued):

Sewer Fund - financed primarily by user charges, this fund accounts for the construction and operation of the municipal sanitary sewer system and related facilities (SDCL 9-48-2). This fund is a major fund.

c. Measurement Focus and Basis of Accounting:

Measurement focus is a term used to describe how transactions are recorded within the various financial statements. Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus.

The City uses a cash basis of accounting, which is a basis of accounting other than USGAAP. Under USGAAP, transactions are recorded in the accounts when revenues are earned and liabilities are incurred. Under the cash basis, transactions are recorded when cash is received or disbursed.

Measurement Focus:

In the Government-wide Statement of Net Assets and Statement of Activities, both governmental and business-type activities are presented using the economic resources measurement focus, applied within the limitations of the cash basis of accounting as defined below.

In the fund financial statements, the current financial resources measurement focus or the economic resources measurement focus is used, applied within the limitations of the cash basis of accounting.

Basis of Accounting:

In the Government-wide Statement of Net Assets and Statement of Activities and the fund financial statements, governmental and business-type activities are presented using a cash basis of accounting.

The cash basis of accounting involves the measurement of cash and cash equivalents and changes in cash and cash equivalents resulting from cash receipt and disbursement transactions. Under the cash basis of accounting, the statement of financial position reports only cash and cash equivalents. Under the cash basis of accounting, transactions are recorded in the accounts when cash and/or cash equivalents are received or disbursed.

As a result of the use of this cash basis of accounting, certain assets (i.e. capital assets) and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, accrued expenses and liabilities, and capital assets and their related debt) are not recorded in these financial statements.

If the City applied USGAAP, the fund financial statements for governmental funds would use the modified accrual basis of accounting, while the fund financial statements for proprietary fund types would use the accrual basis of accounting. All government-wide financial statements would be presented on the accrual basis of accounting.

d. Deposits and Investments:

For the purpose of financial reporting, "cash and cash equivalents" includes all demand and savings accounts and investments with a term to maturity at the date of acquisition of three months or less.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

e. Capital Assets:

Under the cash basis of accounting, the City's capital assets are considered a cost of the program for which they were acquired, for the amount paid in cash, in the Government-wide financial statements, the Fund financial statements, and the Proprietary financial statements.

g. Long-Term Liabilities:

Under the cash basis of accounting, cash proceeds from long-term debt issuances are recorded as a receipt, while payments to creditors to reduce long-term debts are recorded as a cost of the program which benefits from the financing. Allocations are made where appropriate. Interest costs are not allocated, but are reported as a separate program cost category.

Long-term debts arising from cash transactions of all funds are not reported as liabilities in these cash basis financial statements.

h. Program Revenues:

Program revenues derive directly from the program itself or from parties other than the City's taxpayers or citizenry, as a whole. Program revenues are classified into three categories, as follows:

1. Charges for services – These arise from charges to customers, applicants, or others who purchase, use, or directly benefit from the goods, services, or privileges provided, or are otherwise directly affected by the services.
2. Program-specific operating grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for use in a particular program.
3. Program-specific capital grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for the acquisition of capital assets for use in a particular program.

i. Proprietary Funds Revenue and Expense Classifications:

In the proprietary fund's Statement of Revenues, Expenses, and Changes in Fund Net Assets, revenues and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows. That is, transactions for which the related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

j. Equity Classifications:

Government-wide Statements:

Equity is classified as net assets and is displayed in two components under the cash basis:

1. Restricted net assets – Consists of net assets with constraints placed on their use either by (a) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
2. Unrestricted net assets – All other net assets that do not meet the definition of restricted.

Fund Financial Statements:

Governmental fund equity is classified as fund balance, and may distinguish between Reserved and Unreserved components. Proprietary fund equity is classified the same as in the government-wide financial statements.

k. Application of Net Assets:

It is the City's policy to first use restricted net assets, prior to the use of unrestricted net assets, when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

2. DEPOSITS AND INVESTMENTS

The City follows the practice of aggregating the cash assets of various funds to maximize cash management efficiency and returns. Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

Deposits - The City's cash deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 9-22-6, 9-22-6.1, and 9-22-6.2, and may be in the form of demand or time deposits. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts which exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by Federal Home Loan Banks accompanied by written evidence of that bank's public debt rating, which may not be less than "AA," or a qualified public depository may furnish a corporate surety bond of a corporation authorized to do business in South Dakota.

Investments - In general, SDCL 4-5-6 permits City funds to be invested in (a) securities of the United States and securities guaranteed by the United States government either directly or indirectly including, without limitation, United States treasury bills, notes, bonds, and other obligations issued or directly or indirectly guaranteed by the United States government, or otherwise directly or indirectly backed by the full faith and credit of the United States government; provided that, for other than permanent, trust, retirement, building, and depreciation reserve funds, such securities shall either mature within eighteen months from the date of purchase or be redeemable at the option of the holder within eighteen months from the date of purchase; or (b) repurchase agreements fully collateralized by securities described in (a) and meeting the requirements of § 4-5-9, if the repurchase agreements are entered into only with those primary reporting dealers that report to the Federal Reserve Bank of New York and with the one hundred largest United States commercial banks, as measured by domestic deposits; or (c) in shares of an open-end, no-load fund administered by an investment company registered under the Federal Investment Company Act of 1940, whose shares are registered under the Federal Securities Act of 1933 and whose only investments are in securities described in (a) and repurchase agreements described in (b).

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2008

2. DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk

The risk that, in the event of a depository failure, the City's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. As of December 31, 2008, none of the City's deposits were exposed to custodial credit risk.

Interest Rate Risk

The City does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk

State law limits eligible investments for the City, as discussed above. The City has no investment policy that would further limit its investment choices.

State law allows income from deposits and investments to be credited to either the General Fund or the fund making the investment. The City's policy is to credit all income from deposits and investments to the General Fund. USGAAP, on the other hand, requires income from deposits and investments to be reported in the fund whose assets generated that income except where legal or contractual requirements require investment income to be credited to a fund other than the one associated with the assets. Where the governing board has discretion to credit investment income to a fund other than the fund that provided the resources for investment, a transfer to the designated fund is reported. Accordingly, in the fund financial statements, interfund transfers of investment earnings are reported, while in the government-wide financial statements, they have been eliminated, except for the net amounts transferred between governmental activities and business-type activities.

3. PROPERTY TAXES

Property taxes are levied on or before October 1, of the year preceding the start of the fiscal year. They attach as an enforceable lien on property, and become due and payable as of January 1, the first day of the fiscal year. Taxes are payable in two installments on or before April 30 and October 31 of the fiscal year. The City is permitted by several state statutes to levy varying amounts of taxes per \$1,000 of taxable valuation on taxable real property in the City.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2008

4. LONG-TERM DEBT

Changes in long-term debt for the year ending December 31, 2008:

	Balance 01/01/08	Additions	Deletions	Balance 12/31/08	Due Within One Year
Primary Government:					
Governmental Activities:					
Tax Increment District #1	\$ -	\$ 3,307,500	\$ -	\$ 3,307,500	\$ -
Total Primary Government	-	3,307,500	-	3,307,500	-

Long-term debt at December 31, 2008 is comprised of the following:

Tax Increment Financing Note:

Tax Increment Revenue and System Revenue Bond Series 2008, including interest at 4.5 percent, with interest only payments due June 1, 2009, 2010, and 2011, then semi-annual payments of \$148,400. Secured by a mortgage on the wastewater treatment facility.
 Financed through Tax Increment District #1 fund.

3,307,500

Total Long-Term Debt	\$ 3,307,500
-----------------------------	---------------------

As of December 31, 2008, \$192,500 of the approved \$3,500,000 is available to drawdown from USDA.

The annual requirements to amortize all debt outstanding as of December 31, 2008, are as follows:

	Tax Increment District #1	
	Interest	Principal
2009	91,175	-
2010	149,530	-
2011	224,295	58,249
2012	144,522	152,278
2013	137,593	159,207
2014-2018	572,466	911,534
2019-2023	345,309	1,138,691
2024-2028	76,777	887,541
Total	\$ 1,741,667	\$ 3,307,500

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONTINUED) **DECEMBER 31, 2008**

5. RETIREMENT PLAN

All employees, except for part-time employees, participate in the South Dakota Retirement System (SDRS), a cost-sharing, multiple employer public employee retirement system established to provide retirement benefits for employees of the State of South Dakota and its political subdivisions. The SDRS provides retirement, disability and survivor benefits. The right to receive retirement benefits vests after three years of credited service. Authority for establishing, administering and amending plan provisions are found in South Dakota Codified Law 3-12. The SDRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

General employees are required by state statute to contribute 6 percent of their salary to the plan, while public safety and judicial employees contribute at 8 percent and 9 percent, respectively. State statute also requires the employer to contribute an amount equal to the employee's contribution. State statute also requires the employer to make an additional contribution in the amount of 6.2 percent for any compensation exceeding the maximum taxable amount for social security for general employees only. The City's share of contributions to the SDRS for the fiscal years ended December 31, 2008, 2007, and 2006 were \$2,619, \$2,609 (unaudited), and \$2,200 (unaudited), respectively, equal to the required contributions each year.

6. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the period ended December 31, 2008, the City managed its risks as follows:

Unemployment Benefits:

The City has elected to be self-insured and retain all risk for liabilities resulting from claims for unemployment benefits. During the year ended December 31, 2008, no claims were filed for unemployment benefits.

Health Insurance:

The City reimburses employees for single coverage premiums.

Liability Insurance:

The City joined the South Dakota Public Assurance Alliance (SDPAA), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the SDPAA is to administer and provide risk management services and risk sharing facilities to the members and to defend and protect the members against liability, to advise members on loss control guidelines and procedures, and provide them with risk management services, loss control and risk reduction information and to obtain lower costs for that coverage. The City's responsibility is to promptly report to and cooperate with the SDPAA to resolve any incident which could result in a claim being made by or against the City. The City pays an annual premium, to provide liability coverage detailed below, under a claims-made policy, and the premiums are based on their exposure or type of coverage to the pool to provide coverage for general liability, officials' liability, automobile liability and damage, property damage and law enforcement liability.

CITY OF SUMMERSET

NOTES TO FINANCIAL STATEMENTS (CONCLUDED)
DECEMBER 31, 2008

6. RISK MANAGEMENT (CONTINUED)

The agreement with the SDPAA provides that the above coverages will be provided to a \$2,000,000 limit. Member premiums are used by the pool for payment of claims and to pay for reinsurance for claims in excess of \$250,000 for property coverage and \$500,000 for liability coverage to the upper limit. A portion of the member premiums are also allocated to a cumulative reserve fund.

The City would be eligible to receive a refund for a percentage of the amount allocated to the cumulative reserve fund on the following basis:

End of the City's First Full Year	50%
End of the City's Second Full Year	60%
End of the City's Third Full Year	70%
End of the City's Fourth Full Year	80%
End of the City's Fifth Full Year	90%
End of the City's Sixth Full Year and Thereafter	100%

As of the December 31, 2008, the City has a vested balance in the cumulative reserve fund of \$4,742, which is not recorded in the cash basis financial statements of the City.

The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have never exceeded the liability coverage.

Worker's Compensation:

The City joined the South Dakota Municipal League Worker's Compensation Fund, a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the fund is to formulate, develop, and administer, on behalf of the member organizations, a program of worker's compensation coverage, to obtain lower costs for that coverage, and to develop a comprehensive loss control program. The City's responsibility is to initiate and maintain a safety program to give its employees safe and sanitary working conditions and to promptly report to and cooperate with the Fund to resolve any worker's compensation claims. The City pays an annual premium, to provide worker's compensation coverage for its employees, under a self-funded program and the premiums are accrued based on the ultimate cost of the experience to date of the Fund members. Coverage limits are set by state statute. The pool pays the first \$600,000 of any claim per individual. The pool has reinsurance which covers up to an additional \$2,000,000 per individual per incident.

The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have never exceeded the liability coverage.

7. INTERFUND TRANSFERS

Interfund transfers for the year ended December 31, 2008, were as follows.

	Transfer In	Transfer Out
Tax Increment Financing #1	\$ 5,169	\$ -
Sewer Fund	-	5,169
Total	\$ 5,169	\$ 5,169

A transfer was made during the current year from Tax Increment District #1 Debt Service Fund to the Sewer Fund as a capital contribution for the wastewater treatment facility that was purchased during the current year.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF SUMMERSET

BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS

GENERAL FUND

FOR THE YEAR ENDED DECEMBER 31, 2008

	Budgeted Amounts		Budgetary Basis - Actual Amounts	Variance
	<u>Original</u>	<u>Final</u>		
Revenue:				
<i>310 Taxes:</i>				
311 General Property Taxes	\$ 367,335	\$ 367,335	\$ 397,668	\$ 30,333
313 General Sales and Use Taxes	250,000	250,000	212,627	(37,373)
315 Amusement Taxes	12,000	12,000	16,577	4,577
319 Penalties and Interest on Delinquent Taxes	-	-	5,220	5,220
320 Licenses and Permits	40,200	40,200	45,894	5,694
<i>330 Intergovernmental Revenue:</i>				
334 State Grants	-	-	1,720	1,720
<i>335 State Shared Revenue:</i>				
335.03 Liquor Tax Reversion	6,000	6,000	8,323	2,323
335.04 Motor Vehicle Licenses (5%)	17,800	17,800	14,263	(3,537)
335.08 Local Government Highway and Bridge Fund	-	-	1,310	1,310
338 County Shared Revenue				
338.99 Other	-	-	3,540	3,540
<i>340 Charges for Goods and Services:</i>				
341 General Government	-	-	400	400
<i>350 Fines and Forfeits:</i>				
351 Court Fines and Costs	-	-	2,287	2,287
<i>360 Miscellaneous Revenue:</i>				
361 Investment Earnings	-	-	16	16
363.01 Principal Collected by County	-	-	2,600	2,600
364.01 Maintenance Assessments	-	-	36,413	36,413
369 Other	24,500	24,500	10,739	(13,761)
Total Revenue	717,835	717,835	759,597	41,762

CITY OF SUMMERSET

BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS (CONTINUED)

GENERAL FUND

FOR THE YEAR ENDED DECEMBER 31, 2008

	Budgeted Amounts		Budgetary Basis - Actual Amounts	Variance
	<u>Original</u>	<u>Final</u>		
Expenditures:				
<i>410 General Government:</i>				
411 Legislative	42,455	32,455	38,240	(5,785)
412 Executive	28,177	28,177	27,553	624
413 Elections	931	931	-	931
414 Financial Administration	123,580	123,580	112,352	11,228
419 Other	30,000	30,000	31,018	(1,018)
<i>420 Public Safety:</i>				
421 Police	101,938	111,938	153,415	(41,477)
<i>430 Public Works:</i>				
431 Highways and Streets	272,599	272,599	308,046	(35,447)
432 Sanitation	41,250	41,250	17,825	23,425
<i>450 Culture and Recreation:</i>				
451 Recreation	1,500	1,500	1,100	400
452 Parks	-	-	4	(4)
<i>460 Conservation and Development:</i>				
465 Planning and Zoning	74,405	74,405	25,150	49,255
470 Debt Service	1,000	1,000	-	1,000
Total Expenditures	717,835	717,835	714,703	3,132
 Net Change in Fund Balance	 -	 -	 44,894	 38,630
 Fund Balance - January 1, 2008	 132,537	 132,537	 132,537	 -
Fund Balance - December 31, 2008	\$ 132,537	\$ 132,537	\$ 177,431	\$ 38,630

The notes to the required supplementary information are an integral part of this statement.

CITY OF SUMMERSET

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION DECEMBER 31, 2008

(1) Budgets and Budgetary Accounting

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. At the first regular board meeting in September of each year or within ten days thereafter, the governing board introduces the annual appropriation ordinance for the ensuing fiscal year.
2. After adoption by the governing board, the operating budget is legally binding and actual disbursements for each purpose cannot exceed the amounts budgeted, except as indicated in item number 4.
3. A line item for contingencies may be included in the annual budget. Such a line item may not exceed 5 percent of the total municipal budget and may be transferred by resolution of the governing board to any other budget category that is deemed insufficient during the year.
4. If it is determined during the year that sufficient amounts have not been budgeted, state statute allows the adoption of supplemental budgets.
5. Unexpended appropriations lapse at year end unless encumbered by resolution of the governing board.
6. The City did not encumber any amounts at December 31, 2008.
7. Formal budgetary integration is employed as a management control device during the year for the general fund, special revenue funds, capital projects funds, and debt service funds.
8. Budgets for the general fund and special revenue funds are adopted on a basis consistent with the cash basis of accounting.

(2) GAAP Budgetary Accounting Basis Differences

Financial statements prepared in conformity with USGAAP would present capital outlay expenditure information in a separate category of expenditures. Under the budgetary basis of accounting, capital outlay expenditures should be reported within the function to which they relate. For example, the purchase of a new fire truck should be reported as a capital outlay expenditure on the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances; however, in the Budgetary RSI Schedule, the purchase of a fire truck should be reported as an expenditure of the Public Safety/Fire Department function of government, along with all other current Fire Department related expenditures.

SINGLE AUDIT SECTION

CITY OF SUMMERSET

SCHEDULE OF FINDINGS, QUESTIONED COSTS, AND CORRECTIVE ACTION PLAN DECEMBER 31, 2008

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the cash basis financial statements of the City of Somerset (the City).
2. Several significant deficiencies disclosed during the audit of the financial statements are reported in the Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With Government Auditing Standards. Findings 2008-01 and 2008-02 are reported as material weaknesses.
3. No instances of noncompliance material to the financial statements of the City were disclosed during the audit.
4. One significant deficiency disclosed during the audit of the major federal award program is reported in the Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133. This deficiency is not reported as a material weakness.
5. The auditors' report on compliance for the major federal award programs for the City expresses an unqualified opinion.
6. Audit findings relative to the major federal award program for the City are reported in Part C of this schedule.
7. The program tested as a major program was Water and Waste Disposal Systems for Rural Communities (#10.760).
8. The threshold for distinguishing types A and B programs was \$300,000.
9. The City was not considered a low risk auditee under the criteria established in OMB Circular A-133.

B. FINDINGS – FINANCIAL STATEMENT AUDIT

Significant Deficiencies – Material Weaknesses in Internal Control

Finding No. 2008-01: Financial Statement Preparation

Condition: The City does not have an internal control system designed to provide for the preparation of the financial statements being audited, including the related footnote disclosures. As auditors, we were requested to draft the financial statements and accompanying notes to the financial statements. This circumstance is not unusual in a City of your size. This control deficiency could result in a material misstatement to the financial statements that would not be prevented or detected by your City's internal control system.

Criteria and Effect: It is our responsibility to inform the Council that this deficiency could result in a material misstatement to the financial statements that could have been prevented or detected by the City's management.

Questioned Costs: None

Recommendation: It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

CITY OF SUMMERSET

SCHEDULE OF FINDINGS, QUESTIONED COSTS, AND CORRECTIVE ACTION PLAN (CONTINUED) DECEMBER 31, 2008

B. FINDINGS – FINANCIAL STATEMENT AUDIT (CONTINUED)

Significant Deficiencies – Material Weaknesses in Internal Control (Continued)

Finding No. 2008-01: Financial Statement Preparation (Continued)

Response/Corrective Action Plan: Monthly financial statements are submitted to the City Commission on a regular basis for their review. At such time as the Commission would feel the necessity to require statements prepared by an outside source, the Finance Officer will contact appropriate resources for assistance.

Finding No. 2008-02: Segregation of Duties

Condition: Proper segregation of duties assumes adequate internal control over the safeguarding of assets and the reliability of financial records and reporting. The City has a lack of segregation of duties in various areas. More specifically:

- a. The Assistant Finance Officer has the ability to accept utility and other payments, prepares utility billings, posts utility payments and all City revenue, and makes adjustments to customer accounts.
- b. Payroll is completed by the Finance Officer. No review of these records is made by another individual.

Criteria and Effect: As a result of the above, an inadequate segregation of duties existed over the payroll, banking, and utility functions of the City.

Questioned Costs: None

Recommendation:

- a. The Assistant Finance Officer should not have the capability to post adjustments to customer accounts, as well as accepting payments. These duties should be separated between the Finance and Assistant Finance Officers. The Finance Officer should compare the deposits per the bank statement to the receipt book.
- b. Payroll should be reviewed by the Mayor or City Council member prior to payment, in order to verify that individuals are being paid at the proper rate, hours, and are true employees of the City.

Response/Corrective Action Plan:

- a. The Assistant Finance Officer will prepare a written adjustment form with appropriate documentation for the Finance Officer to use in applying the adjustment amount to the customer accounts.
- b. The Finance Officer compared deposits per the bank statement and the receipt book in 2008 and will continue to do so.
- c. The Mayor reviewed the payroll in 2008 and will continue to do so.

Significant Deficiencies – Not Considered Material Weaknesses in Internal Control

Finding No. 2008-03: Publishing Wages/Raises

Condition: The City did not publish the wages of the wastewater employee hired in November 2008. According to State Statute 6-1-10, a complete listing of all the salaries of all officers and employees and thereafter shall be published once any salary paid to any officer or employee has been added or whose salary has been increased, within 30 days thereafter.

Criteria and Effect: The City should publish the wages to comply with state law.

Questioned Costs: None

Recommendation: In order to comply with state law, we would recommend publishing any changes to wages in the city council minutes within 30 days of the change.

CITY OF SUMMERSET

**SCHEDULE OF FINDINGS, QUESTIONED COSTS, AND CORRECTIVE ACTION PLAN
(CONTINUED)
DECEMBER 31, 2008**

B. FINDINGS – FINANCIAL STATEMENT AUDIT (CONCLUDED)

Significant Deficiencies – Not Considered Material Weaknesses in Internal Control (Continued)

Finding No. 2008-03: Publishing Wages/Raises (Continued)

Response/Corrective Action Plan: The Finance Officer will continue to publish the annual salaries of all employees in January and will publish any changes and raises in 2009.

Finding No. 2008-04: Budgetary Overdraft

Condition: The City has budgetary overdrafts in violation of South Dakota Codified Law 9-21-9, in the following departments:

	<u>Overdraft</u>
General Government - Legislative	\$ 5,785
General Government - Other	1,018
Public Safety - Police	41,477
Public Works - Highways and Streets	35,447
Culture and Recreation - Parks	4

Criteria and Effect: The City did not follow state law.

Questioned Costs: None

Recommendation: The City in the future should complete supplemental appropriations for unbudgeted expenditures.

Response/Corrective Action Plan: The Finance Officer will complete supplemental appropriations for unbudgeted expenditures.

C. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAMS AUDIT

Significant Deficiency – Not Considered a Material Weakness in Internal Control

Finding No. 2008-05: Compliance Reporting

Condition: The City does not have an internal control process to review the preparation and timely submission of reports as required by the Loan Letter of Condition and OMB Circular A-133. Forms required include Forms RD 442-2, Statement of Budget, Income, and Equity and RD 442-3, Balance Sheet.

Criteria and Effect: The City is not complying with loan requirements.

Questioned Costs: None

CITY OF SUMMERSET

**SCHEDULE OF FINDINGS, QUESTIONED COSTS, AND CORRECTIVE ACTION PLAN
(CONCLUDED)
DECEMBER 31, 2008**

**C. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAMS AUDIT
(CONTINUED)**

Significant Deficiency – Not Considered a Material Weakness in Internal Control (Continued)

Finding No. 2008-05: Compliance Reporting (Continued)

Recommendation: We recommend the City develop an internal control process for review of both the preparation and submission of these reports.

Response/Corrective Action Plan: Both the Mayor and the Finance Officer will sign the USDA Rural Development quarterly reports. These reports will be submitted as soon as possible following the end of each quarter.

CITY OF SUMMERSET

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>CFDA Number</u>	<u>Amount</u>
<i>U.S. Department of Agriculture:</i>		
Water and Waste Disposal Systems for Rural Communities (Note 1)	10.760	\$ 3,307,500
Total		\$ 3,307,500

Note 1: This program was tested as a major program.

Note 2: The schedule of expenditure of federal awards is presented on the cash basis of accounting.

OTHER REPORTS



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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

City Council
City of Summerset
Summerset, South Dakota

We have audited the cash basis financial statements of the governmental activities, the business-type activities, and each major fund of the **CITY OF SUMMERSET** (the City) as of and for the year ended December 31, 2008, which collectively comprise the City's basic financial statements, and have issued our unqualified report thereon dated February 1, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiencies described in the accompanying Schedule of Findings, Questioned Costs, and Corrective Action Plan as findings 2008-01 and 2008-02 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, findings 2008-01 and 2008-02 described above are considered to be material weaknesses.

City Council

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards, which are described in the accompanying Schedule of Findings, Questioned Costs, and Corrective Action Plan as 2008-03 and 2008-04.

The City's responses to the findings identified in our audit are described in the accompanying Schedule of Findings, Questioned Costs, and Corrective Action Plan. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the governing board and management of the City of Summerset, federal awarding agencies and pass-through entities, the South Dakota Legislature, and state granting agencies, and is not intended to be, and should not be, used by anyone other than those specified parties. However, as required by South Dakota Law 4-11-11 and OMB Circular A-133, this report is a matter of public record and its distribution is not limited.

A handwritten signature in black ink that reads "Ketel Thorstenson, LLP". The signature is fluid and cursive, with the letters "K", "T", and "L" being particularly prominent.

KETEL THORSTENSON, LLP
Certified Public Accountants

February 1, 2010



Ketel Thorstenson, LLP

Certified Public Accountants

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REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

City Council
City of Summerset
Summerset, South Dakota

Compliance

We have audited the compliance of the **CITY OF SUMMERSET** (the City) with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" that are applicable to its major federal program for the year ended December 31, 2008. The City's major federal program is identified in the summary of audit results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2008.

Internal Control over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

Our consideration of the internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified a deficiency in internal control over compliance that we consider to be a significant deficiency.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as 2008-05 to be a significant deficiency.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the City's internal control. The deficiency described above is not considered to be a material weakness.

The City's responses to the findings identified in our audit are described in the accompanying Schedule of Findings, Questioned Costs, and Corrective Action Plan. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the governing board and management of the City of Summerset, federal awarding agencies and pass-through entities, the South Dakota Legislature, and state granting agencies, and is not intended to be, and should not be, used by anyone other than those specified parties. However, as required by South Dakota Law 4-11-11 and OMB Circular A-133, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP
Certified Public Accountants

February 1, 2010